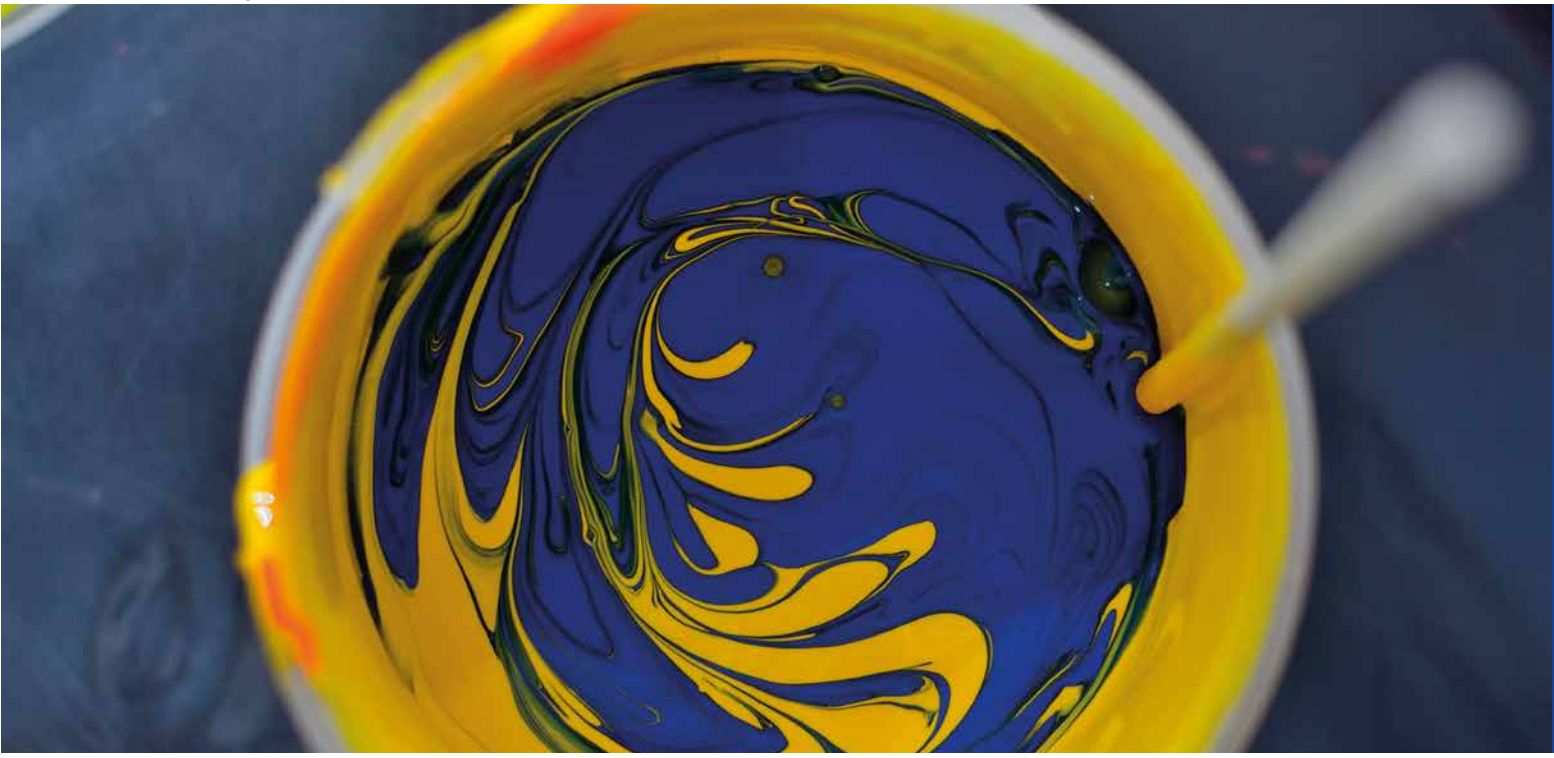
advancing with ESIF financial instruments



Combination of financial instruments and grants

under shared management funds in the 2021-2027 programming period

Factsheet

May 2021

DISCLAIMER

Abbreviations

Abbreviation	Full name
CPR	Common Provisions Regulation
EC	European Commission
EE	Energy Efficiency
EIB(G)	European Investment Bank (Group)
EIF	European Investment Fund
ERDF	European Regional Development Fund
ESF	European Social Fund
EU	European Union
FInt.	Financial Intermediary
FoF	Fund of funds
GBER	General Block Exemption Regulation
GGE	Gross Grant Equivalent
HF	Holding Fund
IFI	International Financial Institution
MA	Managing authority
MFF	Multiannual Financial Framework
NPBIs	National Promotional Banks and Institutions
RDI	Research Development and Innovation
RE	Renewable Energy
SMEs	Small and Medium-sized Enterprises
SPV	Special Purpose Vehicle
TRL	Technology Readiness Level

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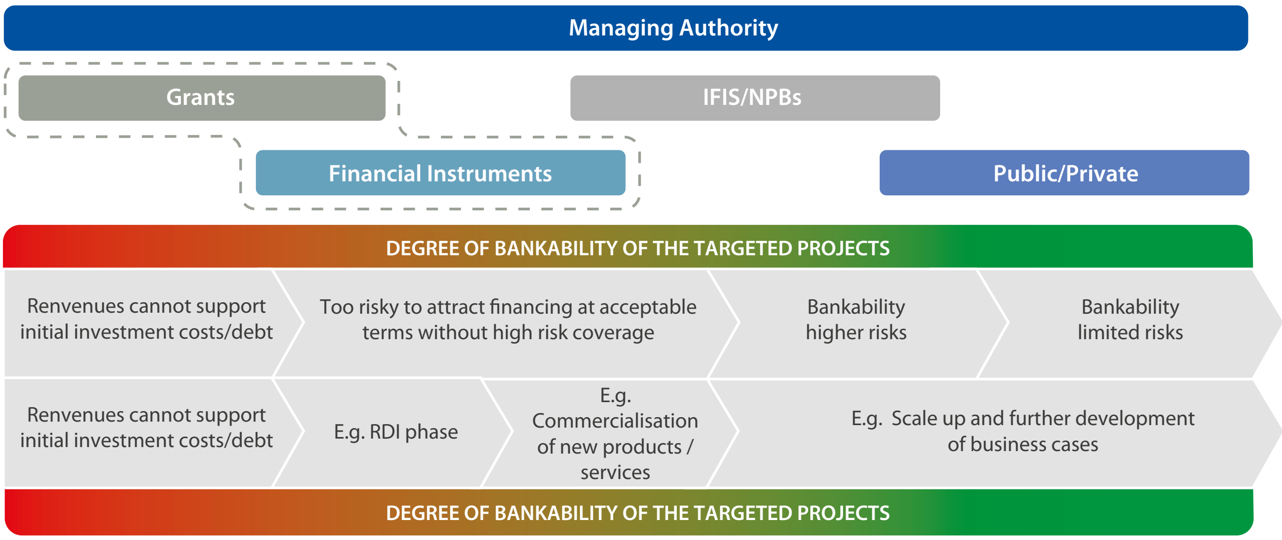
1. Why combine financial instruments and grants?

The combination of financial instruments with grants[1] under shared management can play an important role in delivering EU policy objectives and addressing market failures related to project's design, viability and access to finance issues. Primarily, combinations are needed where investments are not capable of generating sufficient economic returns or cost savings to be viable without additional support. They may also be used to stimulate investment demand, reach ambitious policy objectives and attract private financing. The main benefits of combining financial instruments and grants can be detailed as follows:

- Open up and incentivise entrance to new or riskier markets. Combining financial instruments and grants potentially allows for closing the financial gap to meet the investment needs of transformative projects that would otherwise not be financed through financial instruments only. This is particularly beneficial for projects, which have a high economic, social and/or development impact (for instance the adoption of new technology) but with insufficiently high financial return or too high a risk for private investors (high degree of novelty or level of initial entry costs to the market).
- **Design flexible financial solutions tailored to final recipients' needs**. A combination of grant and financial instruments allows calibrating the repayable form of support in line with expected revenues or savings while maintaining an incentive to deliver a viable project. The combination may answer specific investment projects' needs such as a longer payback period as compared to market standards or an insufficient profitability level in view of market funding costs.
- Combinations of financial instruments and grants may help **structuring projects, which would be more attractive to private investors**. This can be done in several ways such as 'de-risking' the funding structure or demonstrating the long-term viability of specific market segments. Combination may also aim to trigger the development of specific delivery modes or funding structures, which would crowd-in private money (such as investments funds or Public-Private Partnerships) in particular sectors.
- Combinations of financial instruments and grants in a coordinated manner may be **more efficient and generate economies of scale**, by promoting **a one-stop-shop approach**. This may result from increased pooling of funds and a better coordination among stakeholders. An integrated design and screening of projects for the grant and financial instruments components would enhance the coherence of the support instruments.
- Provide **higher incentives for delivery of viable and sustainable investment projects**. Grants may provide less control over the project and create fewer incentives on the promoter to deliver a viable project. Hence, the combination of a financial instrument with a grant maintains the need to generate sufficient revenues for repayment. Combinations may also help develop the pipeline of investment projects to be financed and support more mature and higher quality projects with a deployment timetable of the financial instrument subsequently accelerated.

1 Grants as defined in article 53 ('Forms of grants') of the 2021-2027 CPR.

Figure 1: Indicative financing modes and institutions depending on projects' type and maturity stage



For a sector-specific rationale of financial instrument and grant combinations, see part 3. Sectoral specificities.

2. The 2021-2027 Common Provisions Regulation

2.1 What is new as compared to the 2014-2020 period?

The Common Provisions Regulation for the 2021-2027 programming period (2021-2027 CPR[2]) does not bring changes to the type of investments that are in principle eligible to support from financial instruments. Article 58(2) 2021-2027 CPR states that 'financial instruments shall provide support to final recipients only for investments in both tangible and intangible assets as well as working capital, expected to be financially viable and which do not find sufficient funding from market sources. Such support shall be in compliance with applicable Union State aid rules. Such support shall be provided only for the elements of the investments which are not physically completed or fully implemented at the date of the investment decision'.

In the 2021-27 programming period, 2021-2027 CPR will continue to allow for two types of combination of financial instruments and grant, i.e. in one and in two operations. An important change is the enlargement of the possible options to combine financial instruments and grants in one operation. The rules on combinations of financial instruments and grants are defined in the articles 58(4) to 58(7) of the 2021-2027 CPR as follows:

- Grants can be combined with financial instruments in one single operation (art. 58(5)). In the 2014-2020 period, financial instruments could only be combined with grants in one operation at the financial instrument level, where the grants took the form of an **interest rate, guarantee fee or technical support subsidy. These grants could not be paid directly to the final recipient. The 2021-2027 CPR adds the possibilities to:**
  - use different types of grants under the condition that 'the programme support in the form of grants shall be **directly linked and necessary** for the financial instrument and shall **not exceed the value** of the investments supported by the financial product', and
  - to **make direct payment to the final recipients** (and not only to the benefit of the final recipients as in the 2014-2020 period).
- Grants can also be combined with financial instruments in two separate operations (art. 58(4)) at the level of the final recipient as in the 2014-2020 period.
- In the 2021-2027 programming period, market failures and investment needs will be taken into account and forms of support (financial instruments and grants) will be justified at programme level (art. 22(3)).

2 It is anticipated that the new Common Provisions Regulation will be adopted in 2021.

2.2 Combination of financial instruments and grants in one operation

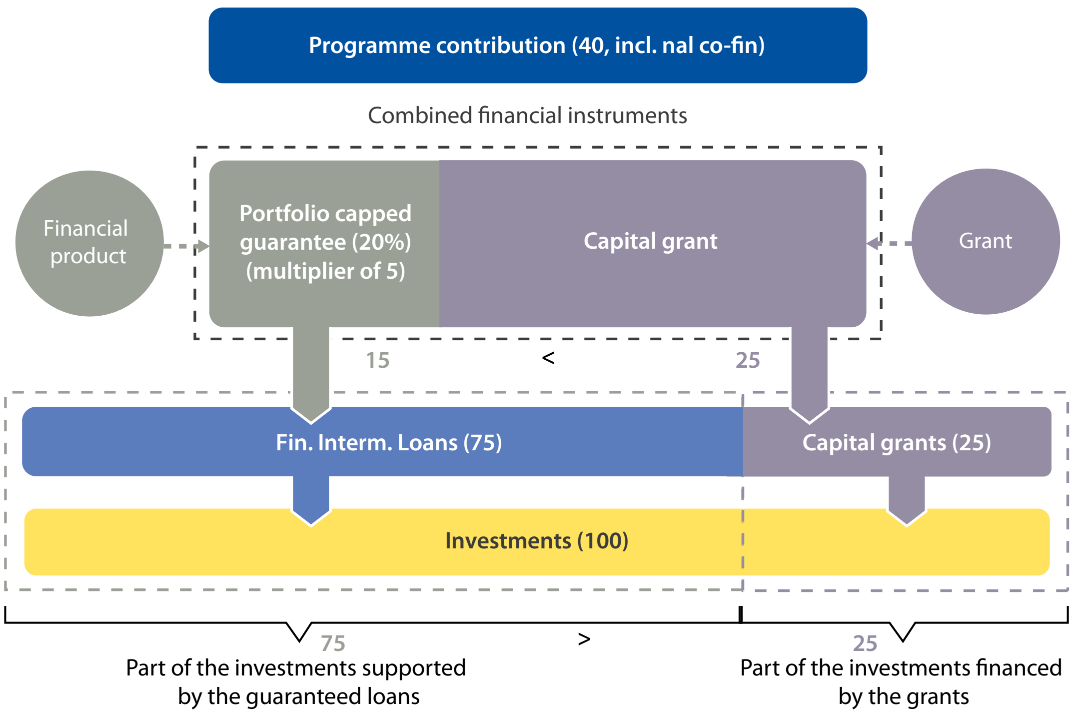
Under the 2014-2020 programming period, 2014-2020 CPR[3] already allowed for the combination of financial instruments and grants in a single operation, provided that grants were used for technical support or to subsidise interest rates and guarantee fees. While keeping these possibilities, 2021-2027 CPR extends the combination options and allows the disbursement of the combined support directly to final recipients. Article 58(5) 2021-2027 CPR states: 'Financial instruments may be combined with programme support in the form of grants in a single financial instrument operation, within a single funding agreement, where both distinct forms of support shall be provided by the body implementing the financial instrument. In such a case, the rules applicable to financial instruments shall apply to that single financial instrument operation. The programme support in the form of grants shall be directly linked and necessary for the financial instrument and shall not exceed the value of the investments supported by the financial product'.

Under 2021-2027 CPR, the combination of financial instruments and grants in one operation remains subject to a series of conditions as follows:

- **The programme support in the form of grants shall be directly linked and necessary for the financial instrument operation**. Article 37(7) 2014-2020 CPR already required the grant combined with a financial instrument in one single operation to be 'directly related to the financial instrument targeting the same final recipients'. This meant that the grant should be part of a single financial package, target the same final recipients as well as facilitate and enhance the financial instrument's impact. In the 2021-2027 programming period, the managing authority needs to demonstrate that the grant is necessary for the financial instrument to, for instance: cover the non-financially viable part of the investment; incentivise for a maximisation of the policy impact (e.g. performance related conditions); mitigate project risks; attract additional private financing; address larger market failures; and/or enhance the coherence and efficiency of support schemes through an integrated one stop-shop-approach.
- **The programme support in the form of grants shall not exceed the value of the investments supported by the financial product**. This condition should be verified at each financial instrument level and not systematically at project level. However, most projects benefiting from this type of combination are expected to report a funding structure in which the investment amount supported by the repayable form of financing (financial instrument) is at least as high as the one covered by the non-repayable one (grant). The value of the investments supported by the financial product - and not the financial product amount itself - is taken as a point of comparison for the grant element. Indeed, in the case of a guarantee financial instrument combined with a grant, the Fund's amount provided as a grant may be higher than the Fund's amount set aside for the guarantee to cover the underlying loan granted to the same project (see example below). This is because the programme contribution to a guarantee financial instrument only covers a percentage of the underlying guaranteed loans though the latter are considered fully EU-supported. Finally, the value of the investments financed by the guaranteed loans should be higher that the value of the grants on a consolidated basis at financial instrument level.

3 Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006.

Figure 2: Example of a guarantee financial instrument combined with a capital grant



- The 2021-2027 CPR allows that, in some limited cases, final recipients get a **higher support from grants than from the financial product** provided the programme support in the form of grants does not exceed the value of the investments supported by the financial product at financial instrument level. This provision offers **flexibility to design** combined financial instruments able to address the **diversity of potential final recipients** and to ensure that the financial instrument reaches ambitious policy objectives.

  Let us take some examples. When grants for technical support are combined with a financial instrument in a single operation, there may be cases, where the technical support financed by the grant does not trigger an investment supported by the financial product. This would be acceptable on an exceptional basis under 2021-2027 CPR.

  Another case could be that a subset of the targeted final recipients cannot afford to repay financial instrument support. This would be typically the case of low-income tenants in multi-apartment buildings the energy efficiency retrofit of which is financed by a financial instrument combined with grants. Without financing these low-income tenants, the overall energy efficiency retrofit project could not be carried out. In this case, low-income tenants could be mostly (or even totally) supported through grants while the remaining tenants would receive a financing package combining grants and financial instruments. This would incentivise tenants to vote for the renovation works and the entire building to be renovated. At financial instrument level, the amount of the investments supported by grants would remain lower than the ones supported by the financial product.

- The rules applicable to financial instruments shall apply to the single financial instrument operation. The combination in one operation provides simplification thanks to the application of a single set of rules of the financial instrument to both the financial product and the grant parts. This means in practice that:
  - The grant and the financial instrument shall both be identified and justified in the programmes as well as further analysed and detailed in the subsequent ex-ante assessment.
  - The grant element will not be a separate operation per se, but part of the financial instrument operation.
  - The substantiation of eligible expenditure will follow financial instruments rules. Eligibility will be determined at the payment of combined support (not necessarily based on final recipients' incurred expenditure, depending on the decision of the managing authority).
  - Management Costs and Fees shall be calculated on the sum of financial instrument and grant amounts.
  - Payment, reporting and audit will follow financial instrument rules (separate records will be maintained).
- **Financial instruments and grants shall be covered by a single funding agreement**. The need for grants should be identified and justified as part of the market failure assessment at programme level and be analysed in details in the investment strategy of the combined financial instrument. Managing authorities will then sign one funding agreement with financial intermediary(ies) (FInt.) covering both contributions to the financial instrument and the grant components. Managing authorities will follow financial instruments' rules for providing the grant monies to FInt. and will not need to launch a separate grant call for that purpose. The content of the funding agreement shall be in line with Annex IX of the 2021-2027 CPR. In the case of direct implementation, this should be done in the strategy document produced by the managing authority.
- Both forms of support shall be provided by the body implementing the financial instrument, meaning that the body implementing the financial instrument is expected to manage the financial instrument, to award the grant and to make the combined funding available. Bodies implementing financial instruments are (i) the bodies implementing the Holding Fund (HF) and (ii) those implementing the specific funds. Therefore, in practice, a FInt. may manage the financial product part of a combined financial instrument while the HF would be in charge of managing the grant part. Such flexibility in the implementation organisation may allow FInt. who may be reluctant to manage grants to be candidate to the management of financial instruments combined with grants in one operation.
- **Separate records must be maintained for each form of support**. The body implementing the financial instrument combined with the grant shall ensure a distinct accounting and reporting of the two elements of the support. The reporting for the grant is part of the financial instrument's requirements.
- Applicable **State aid rules** must be respected.

3. Typology of combined financial instruments

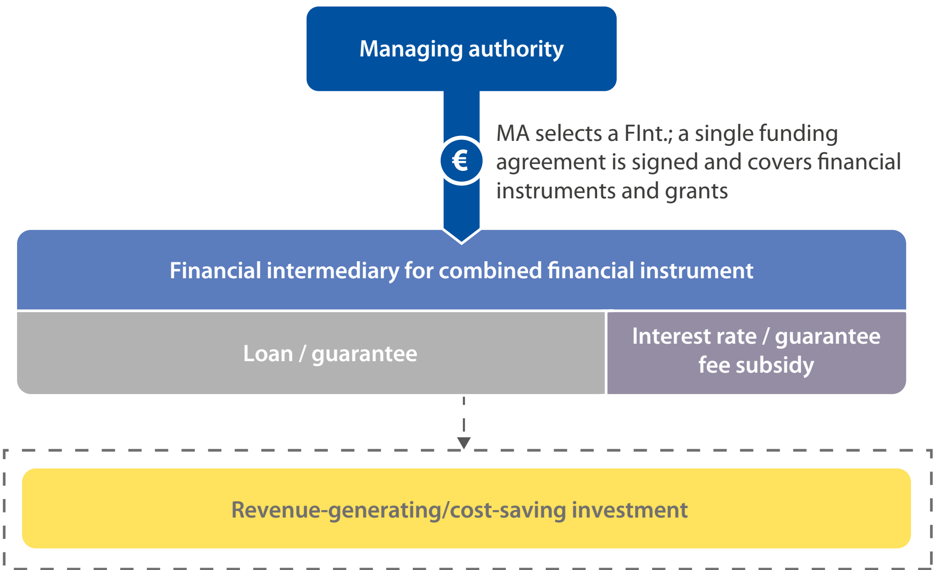
The combination of financial instruments and grants in one operation may follow one of the schemes described below. These examples are not exhaustive. Depending on the observed market failures and on the programme objectives, a managing authority may decide to implement different options.

3.1 Combination of financial instruments and grants for interest rate and guarantee fee subsidies

This option is unchanged as compared to 2014-2020 CPR except that, in the next period, it will be possible to disburse the grant directly to the final recipient (not only for their benefit).

In order to make the best use of the programme contribution transferred to the financial instrument, interest rate and guarantee fee subsidies should be used only to improve the conditions of access to private capital. They should not be used to improve the conditions of the support already received from EU Funds or from national public co-financing through the financial instruments.

Figure 3: Financial instrument combined with grants for interest rate and guarantee subsidies



Example of financial instrument process:

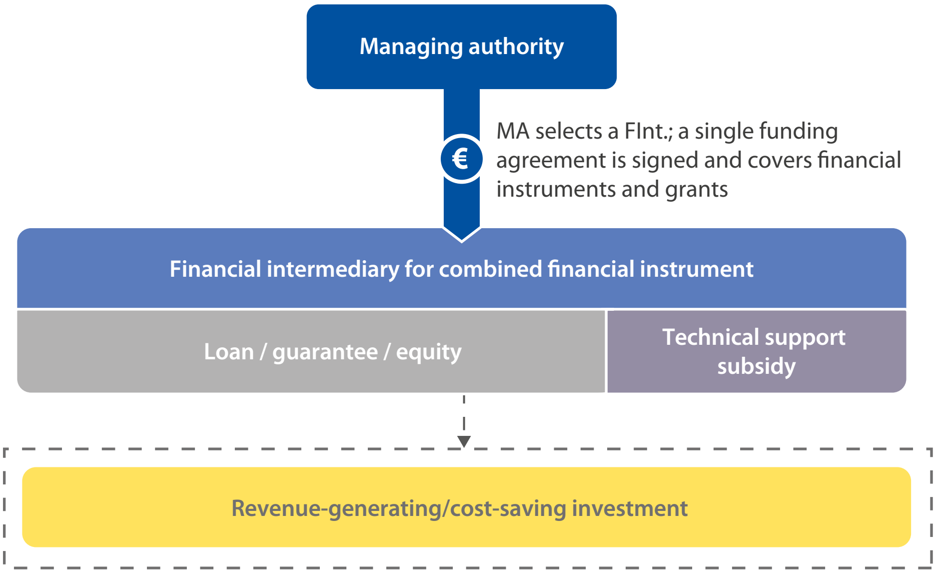
- The managing authority entrusts directly or selects implementing bodies able and willing to manage financial instruments combined with grants.
- A single Funding Agreement covering financial instruments and grants is signed by the managing authority and the FInt..
- In the implementation phase of the financial instrument, final recipients submit a single application to the FInt. for financing.
- In the case of interest rate or guarantee fee subsidy, in the 2014-20 period, the grant had to be directly paid to the bank providing the loan or to the guarantee provider in order to compensate for the lower interest or fee charged. In the 2021-27 period, it will be possible to disburse it to the final recipient to cover part of the interest rate or guarantee fee.

- If interest rate or guarantee fee subsidies are combined with financial products deployed over successive programming periods, the use of escrow accounts to pay subsidies in the subsequent period in respect of financial products paid (e.g. loans granted) in the previous one will not be possible under 2021-2027 CPR. Interest rate subsidies may be further paid in the following programming period if they are in line with the new period's rules and using the new period's resources.

3.2 Combination of financial instruments and grants for technical support

This option is also unchanged as compared to 2014-2020 CPR except that, in the 2021-2027 period, it will be possible to disburse the grant directly to the final recipient (not only for their benefit).

Figure 4: Financial instrument combined with grants for technical support



Example of financial instrument process:

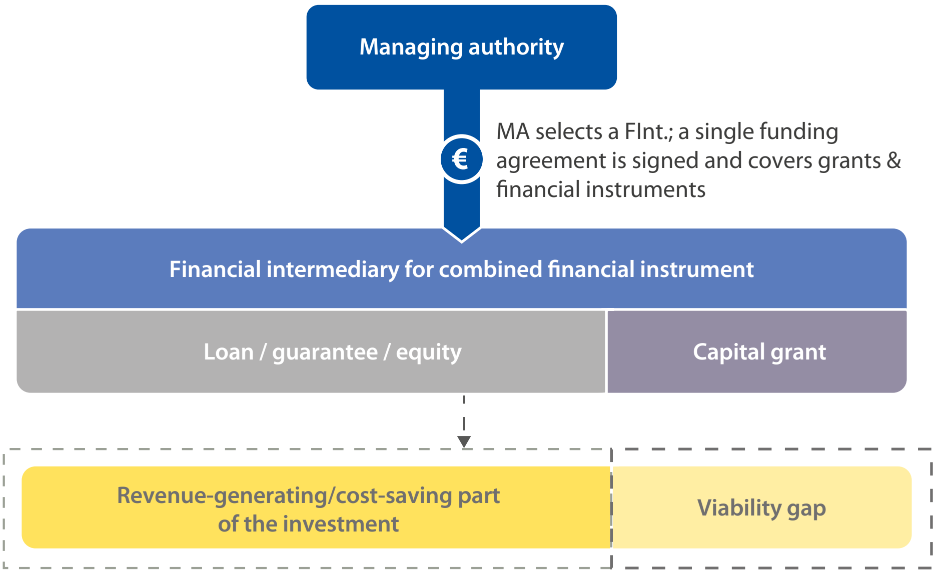
- The managing authority entrusts directly or selects implementing bodies able and willing to manage financial instruments combined with grants.
- A single Funding Agreement covering financial instruments and grants is signed by the managing authority and the FInt.
- In the implementation phase of the financial instrument, final recipients submit a single application to the FInt. for financing.
- The FInt. analyses the project's investment readiness and the potential need for technical support. Technical support can be financed by a grant for the preparation and/or the implementation of the project.
- Two noticeable changes are foreseen by 2021-2027 CPR:
  - Firstly, the technical support grant can be either paid directly to the final recipient or paid on their behalf to cover project preparation and/or implementation costs. A technical support grant could for instance be paid directly to apartment owners to cover the costs of an energy audit in the case of energy efficiency retrofit investment. This energy audit may be performed before and/or after the renovation works.

  - Secondly, at project level, it may be possible that in some exceptional cases, the technical support grant does not lead to a financing from the financial product. In this case, the technical support grant remains an eligible expenditure.
- Once the project is ready, the financial instrument may provide financing in the form of a loan, guaranteed loan or equity investment. As previously mentioned, the technical support grant can be provided alongside the project implementation.

3.3 Combination of financial instruments and capital grants

In this type of combination, the capital grant is intended to cover the non-revenue generating/cost-saving part of the investment. This combination will thus be used to finance investments reporting financial viability gaps.

Figure 5: Financial instrument combined with capital grants



Example of financial instrument process:

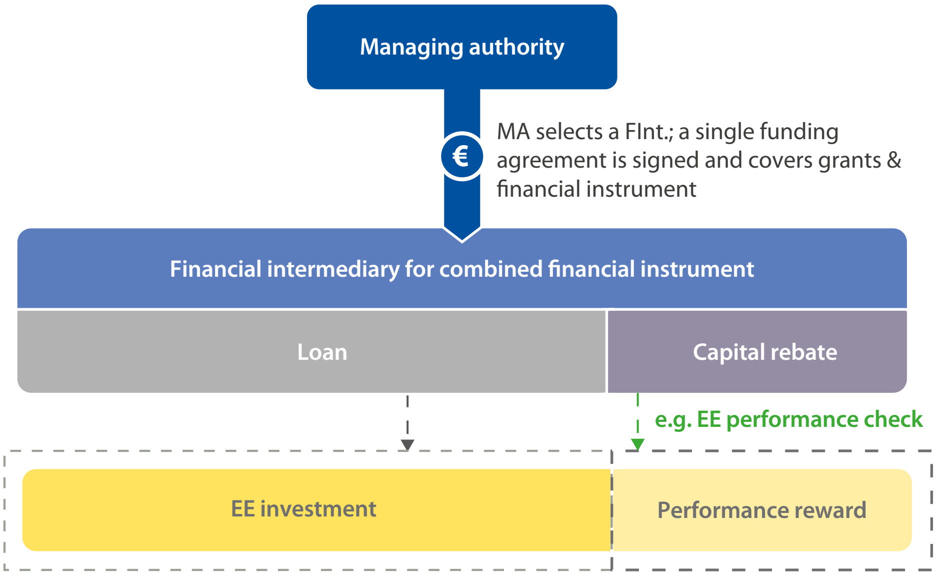
- The managing authority entrusts directly or selects implementing bodies able and willing to manage financial instruments combined with grants.
- A single Funding Agreement covering grants and financial instruments is signed by the managing authority and the FInt.
- In the implementation phase of the financial instruments, final recipients submit a single application for financing to the FInt.
- The FInt. analyses the project's eligibility and financial viability, and in particular the need for a capital grant to carry out the project and the final recipient's capacity to repay the financial product embedded in the combined financial instruments.
- The FInt. decides on both forms of support and makes both forms of funding available to the final recipient. (the grant element could also be managed by the HF as mentioned previously)
- Disbursements may occur either simultaneously or in tranches, depending on the type of project and on the final recipient's funding needs. The disbursement scheme may be decided by the FInt. according to its standard procedures and/or on a case by case basis.
- The grant will not be repaid and will not be used to repay the financial instrument as it should cover distinct expenditure items.

3.4 Combination of financial instruments and performance-based grants

In this type of combination, the grant element will be used to incentivise more project promoters to submit investment projects with a higher policy impact. The type of performance-based grants used may be one of the following. Some others may be chosen provided they remain in line with the conditions defined by the 2021-2027 CPR.

3.4.1 Capital rebates: a part of the loan is converted into a grant

Figure 6: Financial instrument combined with performance based grants



Example of financial instrument process (for energy efficiency investments):

- Managing authority entrusts directly or selects implementing bodies able and willing to manage financial instruments combined with grants.
- A single Funding Agreement covering financial instruments and grant is signed by the managing authority and the FInt.
- In the implementation phase of the financial instruments, final recipients submit a single financing application to the FInt.
- The FInt. analyses the project's eligibility and financial viability.
- The loan contract signed with the final recipient specifies the triggers and amount of the possible capital rebate.
- The project promoter selects a construction company and launches the works. The FInt. pays the final recipient or the construction company based on invoices transmitted by the final recipient.
- At project's commissioning, an independent energy audit is performed. Depending on EE levels achieved, the capital rebate clause in the loan contract is triggered.
- The corresponding part of the capital due to the Fint. is treated as a write-off/an early repayment in the financial instrument's accounts. In case of a risk-sharing loan with private co-financing from the FInt., the latter is entitled to a share of the grants corresponding to its share in the capital rebate. It may also receive early repayment fees on this part.

- The final recipient benefits from a reduction of its capital due and will repay the loan outstanding following a revised amortising plan. In case this capital rebate is applied to a subordinated loan, the consent of senior debt holders may need to be secured as the capital rebate would entail a reimbursement of the subordinated debt, which may be prohibited by senior debt documentation (in particular if the latter was granted as part of an unrelated, previous financial transaction).

How to implement a financial instrument with a capital rebate in the shared management context?

Loan financial instrument combined with a capital rebate

How may a financial instrument combined with a capital rebate be implemented in practice? Let us take the example of the energy efficiency sector. In this field, capital rebates embedded in financial instruments cannot be known with certainty before renovation works are commissioned and audited. In practice, the FInt. may initially provide a loan covering the entire value of the investment supported by the combined financial instruments. If a grace period is foreseen to cover the construction phase, only interests may be paid during this initial phase by the final recipient.

Depending on the level of energy savings actually achieved, part of the loan may be converted into a grant and accounted as a loan write-off or pre-payment by the FInt., thus reducing the latter's credit exposure to the final recipient. A revised repayment schedule of the reduced capital outstanding will then be implemented. Two different situations may be envisaged:

- The Fint. may convert the share of the loan into a grant within the envelope of EU funds it manages, if it is in charge of managing both forms of support.
- The Fint. may also cash in the grant in case it is managed by the Holding Fund.

In both cases, the use of the grant to partly pay back the loan would be in line with 2021-2027 CPR if the eligible expenditure is split between the loan and grant parts and is not declared twice for reimbursement.

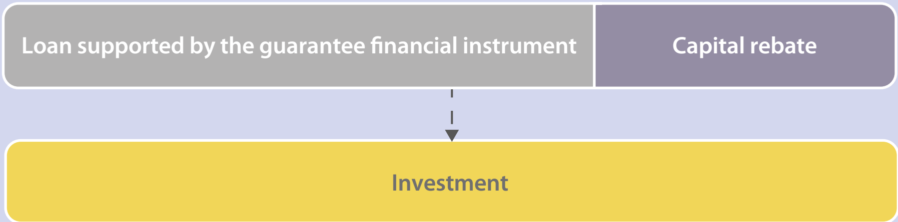
The capital rebate applied to the financial intermediary's part of a risk-sharing loan could also be financed from the loan reflows already paid back to the financial intermediary if any. Otherwise, a part of the Funds (e.g. ERDF) may be set aside to compensate the financial intermediary in case the capital rebate exceeds the part of the loan co-financed by the EU funds and affects the FInt.'s own funds.

An option used by some public development banks is to apply the rebate to the last capital repayments and reduce the loan tenor accordingly. Under this scheme, the final recipient continues to pay back the loan as initially agreed until it is fully amortised, which occurs earlier thanks to the capital rebate. Should banks not find capital rebates attractive against their loans as they would reduce their return on investment, an option could be for them to include in their proposals early redemption fees for parts of the loan that benefit from the rebate. The other option would be for banks to charge a premium on all loans to compensate for the potential rebates. However, banks may accept this high probability of write-off or early repayment as a key feature of the combined financial instrument and consider it anyhow attractive as it may open new markets and (significantly) increase the demand for financing on the ground while reducing credit risks.

From an eligibility point of view, the overall sum eligible for repayment from the EU budget would remain the same before and after the capital rebate, as a part of the loan would be transformed into a grant but without any increase or reduction of the overall support amount at the end of the period. The managing authority will maintain separate records for both forms of funding when declaring eligible expenditure to EC.

Guarantee financial instrument combined with a capital rebate

In the 2021-2027 programming period, a guarantee financial instrument and grants in the form of capital rebates may be combined when they are both co-funded from EU shared management funds. This would be possible under the condition that the **guarantee and the capital rebate support distinct eligible expenditure** and that the grant is not used to reimburse the loan, to avoid double financing of the same expenditure. This means that the underlying investment has to be split between the guaranteed loan and the grant part used in the form of a capital rebate. Consequently, the guarantee will be calculated only on the part of the loan, not the entire underlying investment. In practice, when the initial loan is granted, an amount corresponding to the future capital rebate will not be guaranteed.

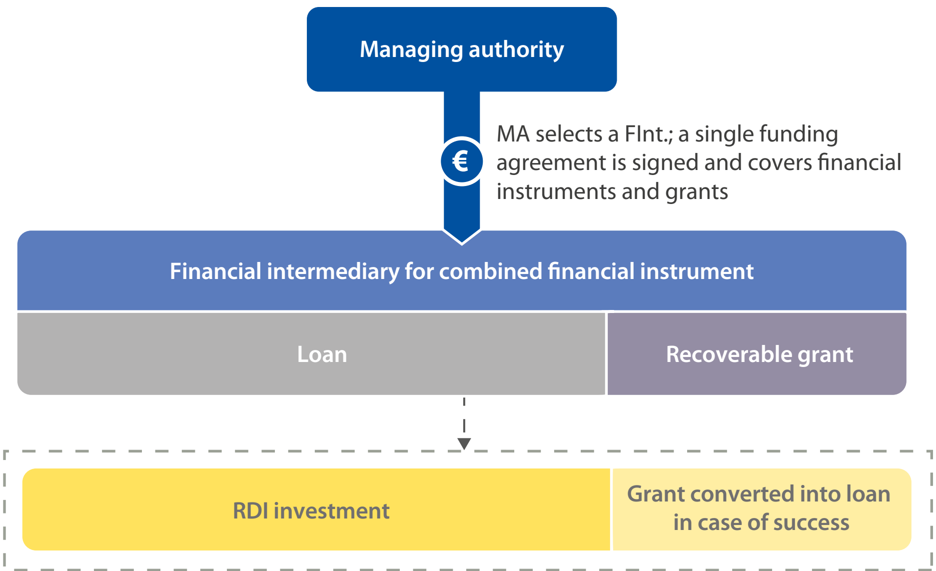


This option implies that when the managing authority makes a programme contribution to the financial instrument, the body implementing the financial instrument knows which proportion is for capital rebate and calculates the necessary guarantee on the amount of the loan portfolio without the capital rebate. An alternative would be that when the percentage of the capital rebate is not known in advance (for instance, if it is performance-based), the guarantee is calculated on the entire loan portfolio and when capital rebates are given, the amount of the guarantee is decreased.

3.4.2 Recoverable grants: a part of a grant is converted into a loan

With a convertible grant, the investor/ financial instrument provides the organisation/final recipient with a grant that is converted into equity or debt if performance objectives are reached.

Figure 7: Financial instrument combined with a recoverable grant

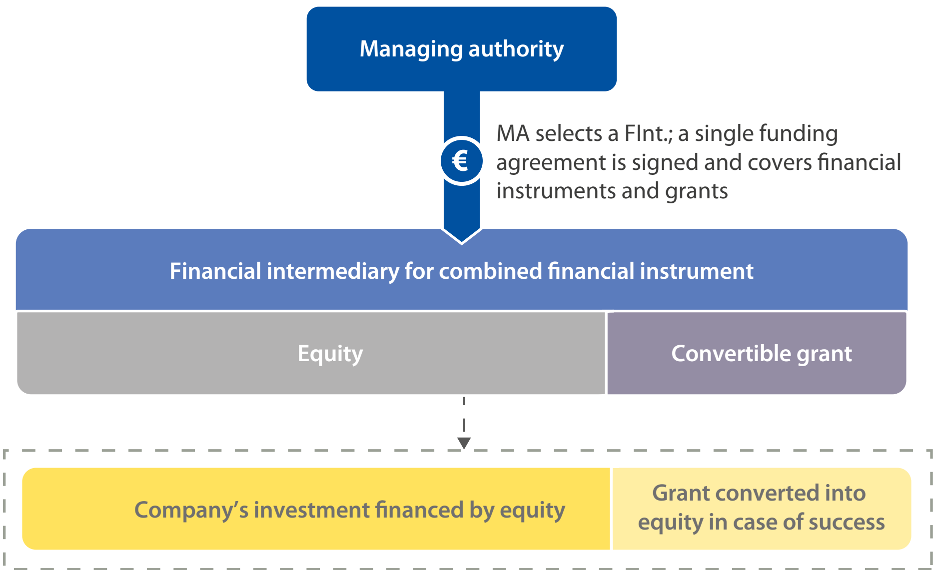


Example of financial instrument process:

- The managing authority entrusts directly or selects implementing bodies able and willing to manage financial instruments combined with grants.
- A single Funding Agreement covering financial instruments and grants is signed by the managing authority and the FInt.
- In the implementation phase of the financial instrument, final recipients submit a single financing application to the FInt.
- The FInt. analyses the project's eligibility and financial viability, approves it, originates the initial loan and provides the performance-based grant, in this case a recoverable grant.
- Project objectives and grant repayment triggers are agreed in the financing contract and are monitored by the FInt..
- If the objectives are reached, the performance-based grant element is triggered. In case of recoverable grant, the grant element (or part of it) is converted into debt and is repaid with the initial loan part following a revised amortisation plan. If the objectives are not reached, the recoverable grant part does not need to be repaid.
- The potential impact of the transformation of the grant part into debt may have an impact on the loan security structure. In case additional collateral for the new debt part would be required from the FInt. (having in mind though that debt financial instrument usually distinguish themselves from market loans by a lower level of collateral required), the initial collateral documents would have to be drafted in such way allowing for possible adjustments during the project's life. The capacity of the final recipient to provide additional collateral should also be assessed when the financing is initially granted, if the debt financial instrument requires the provision of any collateral.
- Besides, should the grant be transformed into subordinated debt, this may require the agreement of the senior debt holders as the senior debt documentation may prohibit such debt increase (in particular if the senior debt was granted as part of an previous unrelated financial transaction).

3.4.3 Convertible grants: a part of a grant is converted into equity

Figure 8: Financial instrument combined with a convertible grant



Example of financial instrument process:

- The managing authority entrusts or selects implementing bodies able and willing to manage financial instruments combined with grants.
- A single Funding Agreement covering grant and financial instruments is signed by the managing authority and the FInt.
- In the implementation phase of the financial instrument, final recipients submit a single financing application to the FInt.
- The fund manager analyses the project's eligibility and financial viability and approves it.
- The decision is made by the fund manager on both the equity and the convertible grant part. The conditions to convert the grant into equity are clearly set up in the investment documentation.
- The fund manager makes the investment in the company and disburses the grant.
- If the objectives are reached, the performance-based grant element is triggered. The grant is (partially) transformed into equity, thus increasing the shares held by the financial instrument. If the objectives are not reached, the convertible grant part does not need to be repaid.

3.5 Combination of financial instruments and grants in two operations

As far as the possibility to **combine financial instruments and grants in two separate operations** is concerned, article 58(4) 2021-27 CPR states that 'support to final recipients may be combined with any form of union contribution, including from the same Fund and may cover the same expenditure item. In that case, the Fund's financial instrument support, which is a part of a financial instrument operation, shall not be declared to the Commission for support under another form, another Fund or another instrument'. The main conditions for this type of combination remain as follows:

- Combination of support shall be done at final recipient level and is not possible at financial instrument level.
- Each form of support remains submitted to its own rules (eligibility, payment,…).
- Financial instruments and grant may cover the same expenditure item but eligible expenditure shall remain distinct. This shall be ensured through the identification of distinct sub-expenditure items or by applying a pro-rata approach with an adequate audit trail.
- Combined support shall not exceed the total expenditure amount.
- Financial instruments cannot pre-finance grants and grants cannot repay financial instruments.

The requirement for separate operations does not prevent both forms of support from being delivered through the same body. Two practical options exist in the 2014-2020 period: the FInt. can either be designated as **intermediate body**[4] for the grant **or** become the **beneficiary** of the grant and redistribute the latter in the form of micro-grants with the financial instrument.

4 'intermediate body' means any public or private law body which acts under the responsibility of a managing authority, or which carries out functions or tasks on behalf of such an authority (Article 2 2021-2027 CPR). The managing authority may identify one or more intermediate bodies to carry out certain tasks under its responsibility. Arrangements between the managing authority and intermediate bodies shall be recorded in writing (Article 71 2021-2027 CPR).

During the 2014-2020 period, some managing authorities have set up financing schemes following **a one-stop-shop approach** for final beneficiaries. It has been the case for instance of the combined loan programme for SME in Hungary or of the combined loan programme for energy efficiency in residential housing in Estonia.

Some of the 2014-2020 combinations under two sets of rules will be possible to be implemented in one financial instrument operation in the 2021-2027 period as explained before. This option of combination in two separate operations may continue to be used for investments where the grant does not fulfil the conditions explained above for one operation (e.g. size of the grant needed for infrastructure projects) or where there is a need that the grants are delivered by the managing authority. Also, any combination with other Union forms of support at the level of the investment has to be done in two separate streams, in particular in case of support through a loan guaranteed under InvestEU and a grant from shared management funds.

4. Sectoral specificities

The following sectoral sections are only examples of where combination may be applicable and are not intended to limit the scope of applicability to other situations.

4.1 SME competitiveness and innovation

4.1.1 Rationale for combination

When it comes to financing research and innovation, a combination of financial instruments and grant can be necessary to ensure the financial viability of investment projects and the successful delivery of the financial instrument. The combination of financial instruments and grant is particularly relevant for RDI given the uncertainty of projects' outcomes, which are not always sufficient to generate a sound stream of cash flows. Research infrastructure also tends to have significant viability gaps that can be bridged only by covering part of the capital investment with a grant. While a large part of the research infrastructure may be covered by grants, a part of the investments for the equipment may be reimbursed by charging users or by commercialising future licences and patents. When the financial viability is ensured but the project still faces difficulties in accessing commercial finance, a grant can be used.

SME investment in innovative products, services, processes or expansion into new markets may also need grant support to mitigate financial risks related to projects' uncertain future cash flows. The adequate funding structure of SME innovative projects depends on the development stage:

- **Creation (start-up) and early growth phase**: until proof of concept stage, it is generally recommended to finance projects with grants. For well-established SMEs bringing innovations to the market, repayable finance (e.g. Venture Capital) may however be combined with grants.
- **Commercialisation phase**: once the proof of concept stage has been successfully reached, some potential for revenue generation can be assessed but risks associated with bringing innovation to the market remain significant. At this stage, projects may need a combination of grants, equity financing and/or senior/subordinated loans.
- **Scale-up phase**: in this phase, to scale up business activities and to enter new markets, SMEs need access to equity and to debt financing with preferential conditions. For risky projects, grants can be usefully combined with equity or debt support.

4.1.2 Product types

Grant type - examples	Financial product type - examples
• **Technical support grant** to cover initial RDI costs, property rights costs (patent, utility scheme), capacity building, marketing studies, business plan. • **Interest rate/guarantee fee subsidy** to lower the cost of borrowing of SMEs with higher risk profile. • **Capital grant**: to cover sunk costs, reduce debt burden, increase loss absorbing capacity. • **Capital rebate**: to incentivise promoters to undertake riskier RDI investments. It can be linked to the achievement of project milestones. • **Recoverable grant**: grant element to be (partly) repaid if project milestones are reached and show revenue-generating/cost-saving potential. • **Convertible grant**: grant converted into equity if projects successfully develop; it offers an upside to managing authorities.	• **Equity investments**: venture capital for companies exploiting RDI results or expanding their activities. • **Short-term loans** for working capital needs. • **Subordinated loans** providing patient capital to SMEs, thus reinforcing the latter's equity structure, without affecting shareholders' breakdown. • **Long-term senior loans** (risk-sharing loans) with a grace period, lower collateral requirements and/or subsidised interest rates. • **Guarantees to FInt.**, which provide loans to growing and to research-and innovation-driven SMEs.

4.1.3 Examples of combination

RDI	**Spain: combined loan for RDI,** managed by the Spanish Centre for the Development of Industrial Technology (CDTI). **No EU funds involved.** This scheme supports investment in research by SMEs. In practice, the support is focused on solvent companies with record of accomplishment and less on start-ups (specific grant instrument has been created for the latter). The financial instrument consists of a **partially reimbursable loan** funded with central State budget resources. It **combines a grant and a loan** as follows: • Loans cover 75% to 85% of the research project, of which 10% to 33% can be rebated • 25% of the loan disbursed upfront, then disbursed according to milestones (case by case basis) This combination could be implemented with EU funds in the 2021-2027 period, provided all other CPR rules are respected, notably the fact that the loan financial instrument should not be used to pre-finance grants and grants shall not be used to repay the loan financial instruments.
	Austria: combined loan for RDI managed by the Forschungsförderungsgesellschaft (FFG). **No EU funds involved.** FFG provides SMEs with a combination of a **non-refundable grant and a soft loan** with a fixed interest rate or a guarantee to a commercial loan with the condition that the loan exceeds EUR 1.5m. If the project fails then loans can be converted into grants. The proportion of grants and loans differs based on the size/creditworthiness of the company. Grants usually account for 20%-40% and in some cases go up to 80% of the loan. Start-ups get a higher grant share. In the 2021-2027 programming period, this type of financial instrument could be implemented using EU funds under shared management in the form of a combination in one operation of a loan and a performance-based capital rebate.
	Germany (Brandenburg): ProFIT, ERDF co-financed financial instrument, Research, Innovation and Technology Promotion Program for SMEs and research institutions, IBB (2014-20) This programme aims to increase the innovation intensity of the Brandenburg economy in terms of sustainable, new or improved products, processes and services as well as cooperation between science, industry and technology transfer. It is delivered through **ERDF co-financed non-repayable grants and/or subsidised loans** depending on the innovation phase. **Grants are up to EUR 3m** per project and can be provided in the **industrial research phase**, for process and organizational innovation and for feasibility studies. Research institutions can also be supported with a grant for the phases of industrial research and experimental development. The **phases of experimental development and market preparation/launch** are in principle supported by **low-interest loans** as far as SMEs are concerned. Loan support is up to EUR 3m per project. **Loans and grants can be combined** and cover up to 100% of the eligible expenses. In the 2021-27 programming period, such financial instrument could be implemented through the combination of a capital grant and a loan in one operation.
Circular economy	**France (Hauts-de-France): CAP 3RI financial instrument, ERDF co-financed financial instrument (2014-2020)** This financial instrument provides financial support to start-ups and mature SMEs active in circular economy, mobility as well as renewable energy, in the form of subordinated loans (EUR1 to 3m) **combined with a technical support subsidy for investment preparation**. This grant can go up to EUR 100k per company. The Fund has a EUR 40.5m size and a dedicated technical support envelope of EUR 2.5m. The financial intermediary operates under the market economy operator principle. In the 2021-2027 programming period, the 2021-2027 CPR will give more leeway to manage the technical support grant combined with the financial instrument in one operation.

<table>
<tr>
<td>Bio-based and blue economy</td>
<td>
EIB Innovfin Advisory services published in 2017 a study dedicated to the 'Access-to-finance conditions for Investments in Bio-Based Industries'. Based on surveyed samples of EU projects, this study notably analysed the typical funding needs of bio-based and blue economies industries by Technology Readiness Levels (TRL) for the purpose of creating a dedicated investment platform. This study provides an interesting benchmark for combined financial instruments in these sectors.
<table>
<tr><td>Bio-based industries (25 projects)</td><td>TRL 6-7</td><td>TRL 7-8</td><td>TRL 8-9</td></tr>
<tr><td>Grants</td><td>42%</td><td>16%</td><td>12%</td></tr>
<tr><td>Equity</td><td>19%</td><td>36%</td><td>37%</td></tr>
<tr><td>Debt</td><td>39%</td><td>42%</td><td>49%</td></tr>
<tr><td>Blue economy (sample of 15 projects)</td><td>TRL 5-7</td><td>TRL 7-8</td><td>TRL 8-9</td></tr>
<tr><td>Grants</td><td>48%</td><td>35%</td><td>8%</td></tr>
<tr><td>Equity</td><td>28%</td><td>40%</td><td>60%</td></tr>
<tr><td>Debt</td><td>24%</td><td>26%</td><td>32%</td></tr>
</table>
Source: Innovfin Advisory
TRL 6: technology demonstrated in relevant environment, TRL 7: system prototype demonstration in operational environment, TRL 8: system complete and qualified, TRL 9: actual system proven in operational environment.
Source: HORIZON 2020
</td>
</tr>
</table>

4.1.4 References

- Spain combined loan for RDI
  http://www.cdti.es
- Austria combined loan for RDI
  https://www.ffg.at/
- Germany, Brandenburg, ProFit
  https://www.ilb.de/de/wirtschaft/darlehen/profit/
- France, Hauts-de-France, CAP 3RI
  http://www.cap3ri.com/
- Access-to-finance conditions for Investments in Bio-Based Industries and the Blue Economy, EIB Innovfin Advisory, June 2017
  https://www.eib.org/attachments/pj/access_to_finance_study_on_bioeconomy_en.pdf

4.2 Energy efficiency

4.2.1 Rationale for combination

Energy efficiency investments are usually structured in such a way that financing costs are (at least partially) covered by savings on energy expenses. In practice, grants are often necessary for funding parts of energy efficiency projects, particularly those which have very low or negative internal rates of return, or, if needed, for social reasons or deep renovation purposes. Hence, in the energy efficiency sector, grants may be combined with financial instruments to:

- achieve ambitious energy saving targets within an acceptable timeframe. For this purpose, loans may typically be combined with grants. Grants provide incentives for final recipients to engage in deeper renovation projects with higher energy saving impact.
- reduce the cost and burden of repayable financing. Grants may be used as capital grants or as loan capital rebates depending on EE objectives to be reached.
- decrease the perceived level of risks of specific market sub-segments, such as homeowner associations, lower income individuals or energy efficiency projects involving SME and ESCO.

4.2.2 Product types

Grant type - examples	Financial product type - examples
• **Technical support grant** to cover (part) of the project preparation/implementation costs such as coaching or energy audits. Individuals and SME EE investment project pipeline can be significantly developed thanks to project preparation and implementation support measures. • **Interest rate/guarantee fee subsidy** to facilitate access of individuals or SMEs to existing loan financing or guarantee schemes. This may allow mobilising private money towards long-term financial instruments. • **Capital grant** to reduce the investment costs for final recipients in line with their loan repayment capacity or to make the IRR positive, thereby attracting private finance. The grant effectively subsidises projects' positive externalities. • **Capital rebate** to create incentives to reach higher energy efficiency standards. The amount of the rebate will increase with the energy savings achieved and confirmed by audits.	• **Senior loan (risk-sharing)** with a grace period, longer tenor and lower collateral requirements and interest rates. • **Guarantees** to FInt. that provide long-term loans at lower interest rate with lower collateral requirements. • **Energy Performance Contracting** for measures with a shorter payback period. • **Mezzanine debt facilities:** to provide patient capital remunerated in line with project performance as well as loss absorption capacity. Help SMEs access senior debt. No impact on equity structure. • **Equity products:** provide high risk-taking capital for innovative projects (e.g. new technologies). Enable to attract mezzanine and senior financers.

4.2.3 Examples of combination

Residential housing

Lithuania, ERDF co-financed financial instrument for energy efficiency (2014-2020)
Renovation loan financial instrument targeting energy efficiency retrofit investments in residential housing, with a focus on homeowner associations in multi-apartment buildings. The loan FI has been co-funded by ERDF, and is combined with different types of grants as follows:
ERDF interest rate and technical support subsidies at financial instrument level.

- State budget grants to fully compensate for loan capital and interest payments of lower income individuals at project level.
- Capital rebates from State budget at project level:
  - Energy savings of 40% › **capital rebate of 25%**
  - Energy savings of 50% › **capital rebate of 35%**

Estonia, ERDF co-financed EE Renovation Loan financial instrument (2007-2013)
Energy efficiency retrofit investments in residential housing, with a focus on homeowner associations in multi-apartment buildings. Renovation loan financial instrument co-funded by ERDF, which is combined with grants funded by State budget resources, i.e. from proceeds of sale of carbon credits. These grants were provided under a separate scheme but could be used by end final recipients to repay the loan.

- Technical support grants up to 50% for energy audits
- Capital grants depending on the energy savings achieved:
  - Energy savings of 20% to 30%: grant equivalent to 15% of total eligible costs
  - Energy savings of at least 40%, grant of 25% of total eligible costs
- 50% and above: grant of 35% of total eligible costs

Greece, ERDF co-financed financial instrument for Energy Savings in Existing Housing financial instrument (2007-2013)
Programme co-financed by ERDF, consisting of partially subsidised loans combined with non-repayable grants, to support households' energy saving investments. Two products were provided by the Programme:

- (a) a loan with a commercial and a subsidised component and
- (b) a grant as non-repayable support covering part of the investment costs, the cost of the energy audit and of the project consultant.

The proportion of these elements varied depending on the income of the homeowners. The 'Energy Savings in Existing Housing' Programme provided from **15% to 70% non-repayable support**, whereas the remainder was offered as a mandatory partially subsidised loan with no collateral, with or without a guarantor, no loan approval expenses and a minimum maturity of four years or a maximum of six years with one year grace period.

Types of final recipients and incentives offered by the financial instrument

Final recipients	Category A1	Category A2	Category B
Personal Income	≤ EUR 12,000	EUR 12,000 – EUR 40,000	EUR 40,000 – EUR 60,000
Family Income	≤ EUR 20,000	EUR 20,000 – EUR 60,000	EUR 60,000 – EUR 80,000
Incentives	70% grant; 30% partially subsidised loan	35% grant; 65% partially subsidised loan	15% grant; 85% partially subsidised loan

Source: Energy Savings in Existing Housing Programme, Greece, Case Study, fi-compass

The strategy's objective was to either raise the funded households by one energy efficiency class, or to reduce their energy consumption by 30%, as measured by energy auditors before and after implementation. The loan-grant combination was provided to final recipients through four FInt. acting as 'one-stop-shops'. By March 2017, when the financial instrument implementation ended, 51 158 households had been assisted in reducing their energy consumption.

SME	**EBRD, SlovSEFF programmes in Slovakia, no EU Funds involved:** SlovSEFF (Slovak Sustainable Energy Finance Facility) III is a sustainable energy financing facility developed by the EBRD in collaboration with the Ministry of Environment of the Slovak Republic and the Ministry of Agriculture, Food and Environment of Spain, which are funding the programme's incentive payments and technical assistance respectively. Given the nature of the overarching carbon credit transaction, SlovSEFF III seeks to promote the reduction of GHG emissions by introducing a **link between a project's GHG emission reduction potential and the incentive payment level** for renewable energy and industrial energy efficiency projects. In practice, partner commercial financial institutions provide loans, which are combined with capital grants ranging from 5% to 20% of the loan amount.
	Germany, KfW CO_2 emission reduction loan programme, no EU Funds involved Soft Loan programmes for companies, maximum tenor of 10 years, to finance construction of energy efficient buildings or renovation of existing industrial/tertiary ones. **Loans are granted by commercial banks and are combined with an interest rate subsidy and a capital rebate** scheme, whose amount depends on energy savings' level achieved. The **capital rebate may go up to 27.5% and 5% of the loan** amount for renovation measures of existing buildings and new construction projects respectively. In practice, the capital rebate is provided in the form of a **reduction of the loan tenor through a write-off of the last annuities** due by the final recipient.

4.2.4 References

- Lithuania Financial Instrument for energy efficiency in residential housing
  https://www.fi-compass.eu/publication/case-studies/residential-energy-efficiency-financial-instruments-lithuania
- Estonia EE Renovation Loan programme
  https://www.fi-compass.eu/sites/default/files/publications/case_study_renovation_loan_programme_estonia_0.pdf
- Greece Energy Savings in Existing Housing Programme
  https://www.fi-compass.eu/publication/case-studies/case-study-energy-savings-existing-housing-programme-greece
- SlovSEFF
  http://www.slovseff.eu/index.php/en/#
- KfW – Energieeffizienzprogramm
  https://www.kfw.de/inlandsfoerderung/Unternehmen/Energie-Umwelt/Förderprodukte/EE-Bauen-und-Sanieren-Unternehmen-276-277-278/

4.3 Renewable energy

4.3.1 Rationale for combination

Renewable Energy (RE) projects are generally characterised by high up-front capital costs and lower operating costs, which are linked to the nature of the technologies used. Project development costs derive from the extensive use of land, lengthy assessment and data collection procedures or the development of connections to energy grids. When technologies are new, RE projects also face significant risks of delays and increased costs of project development due to technological problems and extended permitting and approval procedures.

As a result, RE projects have a material need for (i) initial financing for development costs and for (ii) long-term financing to spread out investment costs over the asset economic life. Initial cost financing may come from sponsors' own resources or market source of risk capital (e.g. VC funds). Long-term financing depends on banks' ability to raise such funding at an affordable cost and on the availability of investors in search of long-term assets to match their liabilities' profile. Smaller scale projects also face specific challenges due to their specific costs (e.g. high transaction costs) and need to be aggregated.

4.3.2 Product types

Grant type - examples	Financial product type - examples
• **Technical support grant** to cover (part) of the project preparation/implementation costs. • **Interest rate / guarantee fee subsidy** to facilitate access of individuals or SME to existing lending or guarantee schemes. This may be an efficient way to mobilise private money in the form of long-term financing. • **Capital grant** to cover development costs, finance viability gaps and reduce ultimate financial costs to increase project's competitiveness and/or decrease ultimate customer prices. • **Capital rebates** to incentivise promoters to complete projects in a timely fashion or to certain performance level. • **Recoverable grants** that turn to senior or subordinated loans if the project achieves specific milestones indicating sufficient revenue generating/costs saving capacity. Grants may incentivise project promoters to take on marginal/ riskier projects, knowing that some costs are covered if the project is unsuccessful. • **Convertible grant:** the grant may fund pre-investment costs as risk capital and provides incentives for project viability. The grant may not be repaid in case of difficulty of the project, thus preserving other investors. Reversely, the grant may transform into equity if the project succeeds. This would protect the public authority's financial interest, which can later exit through a sale of its shares to other private investors.	• **Long term loans** with a grace period, lower interest rates and collateral requests to reduce the weight of debt servicing costs, notably on the first years' cash flows and spread out investment costs over the asset economic life. • **Guarantees** for projects being part of the less-established RE can unlock their access to finance. Private investors might otherwise not invest due to investments' higher risk profiles or too long investment horizons. Guarantees are more attractive to financial intermediaries having liquidity but facing risk-taking constraints. • **Financing lease** for RE installations. This approach can increase the affordability of removable RE assets. For instance, PVs or biomass boilers can be leased to SMEs and/or households. The advantage is that for removable RE installations, no additional collateral is required from the final recipient. • **Subordinated loans**: by mitigating senior lenders' risk, it can make senior debt less costly or available where it was not. Subordinated debt is generally thought of as a means of increasing the share of equity or quasi-equity in RE projects but it can also be used to extend the term of loans, by starting being repaid after an extended grace period or even after all senior debt. • **Equity**: may catalyse RE projects financed via project finance-type SPV and which struggle to attract equity investors, notably to cover (part of) the development costs.

4.3.3 Examples of combinations

Renewable Energy, environmental protection	**European Energy Efficiency Fund (EEEF)** This instrument is notably backed by the EC and the EIB to provide funding to EE and small scale RE projects. Launched in 2011 with global volume of EUR 265 m, it provides tailor made **debt and equity instruments** to local, regional and national public authorities or public or private entities acting on their behalf. EEEF aims at financing bankable projects in EE (70%), RE (20%) and clean urban transport (10%) through innovative instruments and promoting application of the EPC. A **technical assistance grant support (EUR 20m**) is available for project development services linked to investments financed by the Fund.
	Czech State Environmental Fund (SEF) programme, ERDF co-financed financial instrument (2014-20) This instrument provides financing for investment in the risk management of hazardous substances and addresses the 2014-20 programming period TO 6 – Environment and resource efficiency in the enterprise sector. Though not targeting specifically the renewable energy sector, it may be inspiring for the latter. The instrument provides **soft loans** for eligible projects. The **minimum level of the loan is 35%** and it can reach up to 100% of the eligible expenditure. The loan can be combined with a **capital grant from SEF's resources for up to 25% of the investment**.
	Poland: National Fund for Environmental Protection and Water Management (no EU Funds involved) Using **national funds**, this financial instrument offers a **loan with low interest rates that has an option of a capital rebate**. **Up to 10% of the capital**, but not more than PLN 1m, can be rebated if the final recipient does not benefit from another form of grant. An option of a **capital rebate is activated when at least 75% of the loan is repaid on time and the environmental objectives are met**. The loan is given for up to 15 years, but the tenor can be extended to up to 25 years. The loans can allow for a grace period of up to 18 months.

4.3.4 References

- Eeef
  https://www.eeef.eu/home.html
- Czech State Environmental Fund (SEF) programme
  https://www.sfzp.cz/en/administered-programmes/
- Polish National Fund for Environmental Protection and Water Management
  http://nfosigw.gov.pl/oferta-finansowania/srodki-krajowe/informacje-ogolne/umorzenia/.

4.4 Urban / sustainable infrastructure

4.4.1 Rationale for combination

Urban development investments tend to integrate elements with a high social and/or environmental impact but not generating any (or low) financial return. The latter, if not financed, can potentially create barriers for the successful implementation of key projects (e.g. site decontamination or provision of public or green spaces, renovation of heritage/cultural assets). Urban infrastructure is also generally characterised by material development costs and long-term economic life. In terms of financing, it therefore requires some form of public support to keep ultimate financial costs/ user fees at an acceptable level (if any) and/or long-term forms of financing matching project's life. Combinations of grants and repayable forms of finance have been extensively used - notably outside of the EU Funds world - to finance urban and sustainable infrastructure development. In the next period, this type of combination could be further used with EU Funds' resources in case of market failure. A promising area may be innovative urban investments such as 'smart city' type projects, where EU Funds can play a key role in mitigating technology and innovative business models' related risks, scaling-up pilot projects and attracting private investors. More traditional infrastructure projects may also benefit from these combinations, notably to decrease ultimate costs paid by users.

4.4.2 Product types

Grant type - examples	Financial product type - examples
• **Technical support grant** to finance the project design and preparation. This support may be key in projects employing innovative technologies and/or new business models (e.g. 'smart city'). • **Interest rate / guarantee fee subsidy:** may be used to make long-term financing available / affordable. • **Capital grant** to cover development costs**,** fund viability gaps and reduce ultimate financial costs and ultimate customer prices (e.g. public transport ticket price or waste collection fee). In remote areas, smaller projects may face limited demand and high costs to connect to the network, which can be mitigated by grants. • **Capital rebates** to incentivise developers to complete projects in a timely fashion or to certain performance level. • **Recoverable grants** that turn to senior or subordinated loans if the project achieves specific milestones indicating revenue-generating capacity. Grants may incentivise project promoters to take on marginal/riskier projects. • **Convertible grant:** to cover pre-investment costs and provides incentives for project viability. The grant may not be repaid in case of difficulty, thus preserving other shareholders. On the other hand, the grant may be converted into equity if the project succeeds, thus protecting the public authority's financial interests.	• **Long-term loans** with a grace period, lower interest rates and collateral request to reduce the weight of debt servicing costs, notably on the first years' cash flows. It may help spread out investment costs over the asset economic life, which may above 15/20 years in this sector. Given politically set fee levels, projects need time to break-even. In sectors which do not generate direct streams of revenues but have significant quantifiable externalities (e.g. air quality or flood risk prevention), a long-term debt financing can also be provided, for instance to municipalities. • **Guarantees** to incentivise private lending with lower interest rates and collateral requirements and (much) longer tenors (20 years+). Lenders may require guarantees in particular when borrowers have a limited liability company legal form and are subject to liquidation proceedings. • **Financing lease instrument** for public transport rolling stock material for instance. • **Subordinated loans** to mitigate senior lenders' risks by reducing the share of senior debt in total financing. Subordinated debt may be for instance an efficient way to reinforce the capital of an SPV implementing a 'smart city'-type investment without diluting its equity structure. • **Equity**: for urban investment projects carried out using SPVs or specifically created companies (e.g. revitalization projects with high initial costs). This helps attract private investors reassured by the project's loss absorption capacity.

4.4.3 Examples of combination

<table>
<tr>
<td>Social Housing</td>
<td>In many EU countries, social housing projects combine different funding sources such as commercial and subsidised loans, grants and equity from social housing entities or tenants. This sector has a general need for grants to cover (part of) construction and land costs and reach economic viability. Grants thus help to keep rents at affordable level for lower and middle-income tenants and remain for most social housing institutions an indispensable part of financing. Below are a few examples of the weight of grants used in combination with other sources to finance social housing within the EU.
The study on social housing in the EU entitled 'Eclairages, Logement social et territoires' published by the Banque des territoires (French CDC group) in July 2020 identified various social housing financing models in Europe combining loans, grants and own funds as follows:

Financing plans for social rental housing construction operations
<table>
<tr><th></th><th>Germany</th><th>France</th><th>UK</th><th>DK</th></tr>
<tr><td>Commercial loan</td><td>37%</td><td>7%</td><td>53%</td><td>84%</td></tr>
<tr><td>Public loan</td><td>25%</td><td>71%</td><td>-</td><td></td></tr>
<tr><td>Grant</td><td>-</td><td>9%</td><td>14%</td><td>14%</td></tr>
<tr><td>Own funds</td><td>38%</td><td>13%</td><td>33%</td><td>2%</td></tr>
</table>
Source: CDC</td>
</tr>
<tr>
<td>Municipal investment</td>
<td>Outside of the EU, Green Municipal Fund of the Federation of Canadian Municipalities
Endowed with CAD 414m from the Government of Canada, the Green Municipal Fund supports public and private sector-led initiatives for innovative municipal infrastructure solutions with clear environmental benefits, public value, and model business cases and technologies. It provides support for, on the one hand, (i) plans, feasibility studies and pilot projects and, on the other hand, (ii) capital projects in planning, brownfield, energy, transport, waste and water. The support is a package of grants and low interest loans, where grants are capped at 50% of the costs for plans, feasibility studies and pilot projects and low-interest loans are capped at 80% of the costs for capital projects (the grant amount to 15% of the loan). Since 2000, the Fund has approved (i) 1,045 projects for plans, feasibility studies, and pilots with a grant amount of about CAD 60.2 m and a total project value of about CAD 181m (ratio of 1:3) and (ii) 298 capital projects for CAD 64 m in grants and CAD 461 m in loans for a total project value of CAD 2.6bn (ratio 1:5). In 2016, the Government provided an additional CAD 94m to strengthen the focus on low-carbon, resilient municipalities and asset management.</td>
</tr>
</table>

4.4.4 References

- EU social housing models
  https://www.banquedesterritoires.fr/sites/default/files/2020-09/Eclairages22_WEB_VF.pdf
- Green Municipal Fund of the Federation of Canadian Municipalities
  https://www.adb.org/publications/green-finance-catalyzing-facility

4.5 Not-for-profit entities / social infrastructure

4.5.1 Rationale for combination

Social economy SMEs are generally characterised by limited operating cash flows and a low level of own funds, which constrain their debt taking and investment capacity. A financial product combining a grant aimed at covering part of the investment costs and reinforcing the social enterprise's own funds and a financial instrument providing a repayable financing in line with project's expected cash flows would help those social enterprises grow and expand their activities.

The health, affordable and student housing or child and elderly care sectors report large investment needs while their revenue generating capacity is constrained by user's payment capacities. The latter indeed usually cannot cover the full service costs. A combination of long-term debt and grants may hence be used to finance investment projects in social infrastructure and lower the latter's costs and final price for end-users. Financial markets are also not always offering such long-term debt at an affordable cost due to a limited refinancing capacity or lower risk appetite, in particular to borrowers not benefiting from a public legal status or a sovereign guarantee. A combination of financial instruments and grants may also help cover these funding gaps.

4.5.2 Product types

Grant type - examples	Financial product type - examples
• **Interest or guarantee fee subsidies** in the case of commercial loans to help provide affordable long-term financing. • **Capital Grants:** Non-profit entities, which cannot take on equity may need to raise grants that perform a layered risk function and allow them to take on debt. • **Recoverable grant**: it is a loan, part of which will be paid back only if the project reaches previously defined milestones. If not, the loan is (partly) converted into a grant, for instance via a capital rebate. This mechanism can be used if the successful project enables the social enterprise to repay the loan. • **Forgivable loan**: it is a loan, which is converted into a grant in the case of success of the project. If the social enterprise reaches the goals agreed on beforehand by the investor and investee, the loan does not have to be (fully) repaid. A pre-agreed objective for the social enterprise could be for instance the creation of jobs. • A **convertible grant** is another financing instrument with hybrid capital character. The social investor provides the enterprise with a grant that is converted into equity in the case of success. Otherwise, the grant is not paid back.	• **Guarantees** to incentivise private lenders to make loans to social economy entities at softer conditions or to start lending in social areas where they did not provide financing previously, for instance micro-finance. • **Soft loans** with lower interest rates and lower collateral requirements, with longer tenors for infrastructure partly covered by customer fees and to social economy companies. • **Subordinated loans:** provides patient capital necessary to expand social enterprises' activities and perform a risk layered function in case equity funding is difficult to attract due to limited expected profitability or legal constraints. Enables an easier access to senior debt financing. • **Equity:** depending on the entity's legal status, own funds may be provided in different forms such as corporate shares or specific own fund participation forms (e.g. 'titres associatifs' in France). It remains a key source of funding providing stable and patient capital for the entity's expansion.

4.5.3 Examples of combination

<table>
<tr>
<td>Microfinance</td>
<td>
Hungary: Combined Micro credit and Grant scheme, EDRF co-financed financial instrument (2007-2013)
This financial instrument provided micro-finance to micro-enterprises. The MA allocated EUR 202m of ERDF (85%) and national funds (15%) to the financial instrument, which financed up to 45% of project's costs through a grant and up to 45% through a loan, while SME financed at least 10% through its own contribution. Over 140 micro-financing institutions, local enterprise development foundations and saving cooperatives joined the scheme. 9 389 recipients received combined micro-credit to enhance their businesses and help bridge financing gaps, which previously resulted from the relatively high levels of transaction costs for small credit requests of micro enterprises.
<table>
<tr><th>Own contribution</th><th>Grant</th><th>Loan</th></tr>
<tr><td>Minimum 10%</td><td>Up to 45%
EUR 3,000 to 33,000</td><td>Up to 45%
Maximum EUR 66,000</td></tr>
</table>
Source: Combined Micro Credit and Grant scheme, case study, fi-compass

Financial intermediaries reviewed the applications of final recipients and awarded the loan and the grant. According to the implementation structure, the scheme became a 'one-stop-shop' in which micro-enterprises applied through private financial intermediaries, which financed the micro-credit part, thus reducing the administrative burden for SME. The State-owned holding funds acted as a 'back-office' paying the grant. The two institutions had to evaluate different aspects of the project and shared risks.
</td>
</tr>
<tr>
<td rowspan="2">Social economy</td>
<td>
UK: Social economy convertible grant programme, Nesta, no EU funds involved
Crowdfunder is a UK based crowdfunding platform that helps raise money for various entities such as business ideas, charities, community groups. As of November 2018, it had raised over £50 million for more than 20,000 projects. Crowdfunder has been initially supported by the social impact investor Nesta using a convertible grant (from UK Central Government resources) combined with equity crowd investment and stage-gated funding (NB: a stage-gated funding is a phased grant programme, the different components of which are subsequently disbursed based on the achievement of specific milestones or 'gates').
According to Nesta report, given the uncertainty about the long-term viability of the financial model at the time of the initial investment, a convertible grant was deemed the most appropriate model, balancing the risk of failure with the ability to gain from profitability and to influence Crowdfunder's development by taking a future board role. Initially, the £149,660 grant provided flexibility for the company to focus on what was important for delivering the reward-crowdfunding platform, compared to a loan or equity investment. The convertible grant was then converted into equity in view of the successful development of the company in 2012. Two subsequent equity investments were made by Nesta in 2014 and 2016, thus bringing the overall equity stake managed by the social impact investor to £319,660 in total.
</td>
</tr>
<tr>
<td>
Portugal: Social Innovation Initiative, ESF co-financed financial instrument and grant scheme (2014-20)
This initiative combines several grant schemes and financial instruments. Under this scheme, social innovation and social entrepreneurship projects can get a grant support up to EUR 50 000 (in the form of vouchers) to finance small capacity building plans (up to 18 months of duration). It funds 100% of eligible costs to beneficiaries (85% ESIF-ESF + 15% Portugal State budget) and intends to solve one of the main barriers for impact investing in social innovation or social entrepreneurship projects i.e. the still significant skill gaps and the corresponding lack of investment readiness of most projects. Then project promoters can apply for a financial instrument support from the Social innovation Fund ('SIF').
SIF is structured as a hybrid model of fund with two financial instruments: a debt financial instrument with a wholesale approach, designed to ease the access to finance for the social economy entities and a retail equity financial instrument to foster the social investment market. On the debt financial instrument, SIF will provide guarantees so financial institutions can provide loans to social economy entities at below the market conditions. On the other hand, the equity financial instrument will co-invest alongside private investors in SMEs that are implementing social innovation projects.
</td>
</tr>
</table>

4.5.4 References

- Hungary, combined Micro Credit and Grant scheme
  https://www.fi-compass.eu/publication/case-studies/case-study-combined-micro-credit-and-grant-scheme
- UK, Nesta, convertible grant
  https://media.nesta.org.uk/documents/Funding-Innovation-Nov-18.pdf
- Portugal, Social Innovation Initiative
  https://www.fi-compass.eu/publication/factsheets/factsheet-fi-compass-study-social-impacts-bond-programme-under-portugals

5. Frequently asked questions

5.1 Financial instrument design phase

1. **Must combinations be used only to cover the non-financially viable part (non-revenue generating or non-cost saving) parts of investments?**

   No. The 2021-2027 CPR allows financial instrument/grant combinations in one operation to support projects that are not fully financially viable, i.e. that do not generate sufficient returns or savings to be financially viable. Additionally, it is expected that 'combined financial instruments' will be used to stimulate investment demand, pursue wider policy objectives and/or attract private financing to projects/programmes. Investment grants described in this note may be used not only to cover the viability gap of an investment project but also, for instance, to decrease the burden of the repayable form of finance on the project's cash flows or to reduce the final costs of the supported investment to be covered by user fees.

2. **What should be included at programme level regarding combinations of financial instruments and grants in one operation?**

   In order to identify and justify the grant element adequately, the programme should indicate in general lines why the grant is needed, for instance to cover a financing gap, to support a better structuring or implementation of the projects. There is no need to include in the programme the elements of the ex-ante assessment, but the programme may indicate that the parameters to govern the use of the grant (e.g. the grant intensity methodology) should be established in the ex-ante assessment. The methodology will differ from sector to sector. For example, in the urban development sector, the level of the grants may be determined at a later stage when the projects are identified and the project design is at an advanced stage. For the SME sector, it might be possible to justify fixed grant rates from the beginning.

3. **How to avoid crowding out effects between financial instrument-grant combinations and other financial instruments?**

   In order to avoid a crowding out of financial instruments by financial instrument-grant combinations, it is critical to ensure that that combined financial instruments target well identified market failures and final recipients, for which a combination is expected to make a real difference in terms of policy impact. These combined financial instruments should be proposed under specific conditions, which would differentiate them from other financial instruments potentially set up for the same market. For instance, in Hungary, during the 2014-2020 period, the combined loan and grant financial instrument for SMEs (the financial instrument combined a loan and a grant element covering up to 60% and 30% of the project costs respectively) charged a higher interest rate on the loan (2%) than the loan financial instrument (provided at 0% interest rate). This 'price differentiation' intended to incentivise final recipients to apply for the most appropriate form of support in view of their needs. In the 2021-2027 programming period, managing authority will be required to take into account market failures at programme level and to justify the chosen forms of support (grant vs financial instrument). On this basis, at financial instrument level, the ex-ante assessment and investment strategy should make recommendations regarding the scope, amount and features of the financial instrument needs and forms of financial instrument and grant combinations as well as delimitation issues with other delivery instruments should be addressed at this stage.

4. **In case of a financial instrument combining in one operation grants and a portfolio guarantee financial instrument, where each loan is guaranteed at 80%, how is the amount of investments supported by the financial instrument computed?'**

   In case of a guarantee financial instrument combined with a grant in one operation, the **total amount of investments financed by the guaranteed loan will be considered to be supported by the financial product** part of the combined financial instrument. The actual guarantee rate of the underlying loan will not have any impact on the amount of the investments supported by the financial instrument.

   In case a guarantee financial instrument is combined with a capital rebate, it will be necessary **to split the investment amount between the guaranteed loan and the grant components, meaning that the guaranteed loan will not cover 100% of the investments costs but 100% minus the capital rebate amount.**

   One option, when the proportion of programme contribution that will be applied through a financial instrument as a capital rebate is known, would be to calculate the necessary guarantee on the net amount of the loan portfolio after the capital rebate is paid. For example, In case of an investment of 100, an initial loan of 100 is made and a capital rebate of 30 is anticipated to follow. The guarantee rate of the loan is 80% and, therefore, the amount set aside for the guarantee will be: 80% * (100 – 30) = 56.

   An alternative would be that when the percentage of the capital rebate is not known in advance (for instance, if it is performance-based), the guarantee is calculated on the entire loan portfolio and when capital rebates are given, the amount of the guarantee is decreased.

5. **How will the operation be selected?**

   In combinations in one operation, the selection criteria at the level of the programme applies to the financial instrument operation as a whole, including the grant element and also the eligibility criteria are established for the entire operation (financial instrument and grant).

   In separate operations, where each form of support follows its own rules and where it is not possible to proceed under a single operation approach, it is important to have a clear line between those projects and the expenditure that is eligible for grants and that is eligible for financial instruments. The selection criteria established in line with Article 73 should allow the managing authority to make a clear demarcation between the grant and the financial instrument operations. Further down, at the level of the support provided to final recipients, the eligibility rules for grants could be defined in such a way that their use is limited, in order to favour a wider reach of financial instruments.

6. Do financial intermediaries have to participate in a grant call to be selected as the manager of the grant element within a combined financial instrument in one operation?

No, the bodies implementing a combined financial instrument in one operation shall be selected based on a single procedure, which will simultaneously cover the grant and the financial product parts of the combined financial instrument. This is a major difference with the option of combining financial instruments and grants in two separate operations, where two distinct selection procedures shall apply in line with the two forms of support respective rules.

7. How should the state aid amounts be computed for combinations in one operation?

Under *de minimis,* an overall amount of aid, i.e. in the form of a grant and of a gross grant equivalent (GGE) of the repayable form of support, will be computed. Let us take the example of an eligible investment of EUR 100,000 to be financed by the combined financial instrument in the form of a capital grant of EUR 30,000 and a loan of EUR 70,000. The amount of aid in the form of a grant amounts to EUR 30,000. The GGE calculated on the loan amounts e.g. to 3 000. Finally, the amount of aid of the combination is equal to 30 000 + 3 000 = 33 000. For loans with capital rebates, the grant element could be included in the initial calculation at its value, discounted accordingly. Should the project not perform as expected and the capital rebate not be finally granted, the computation could be adjusted later on.

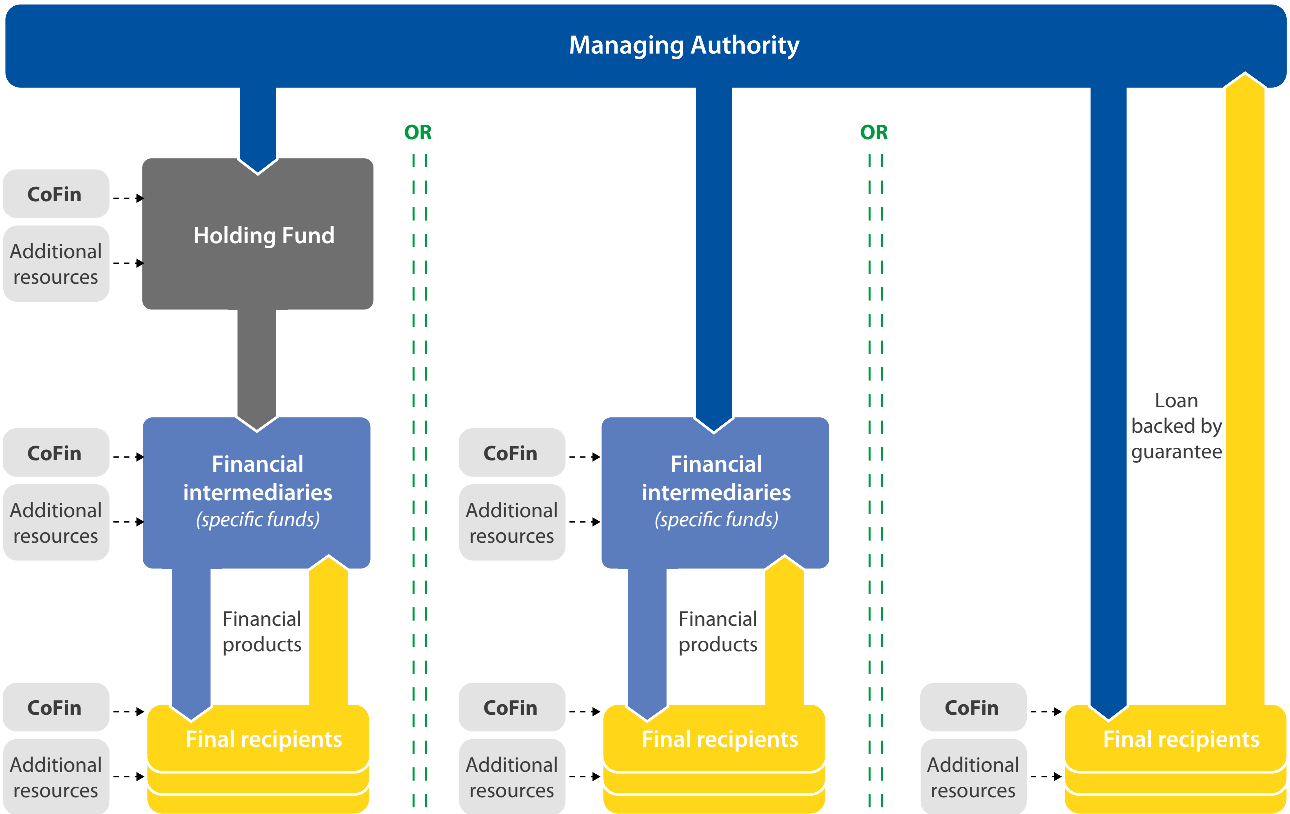
8. What will be the impact of combining financial instruments and grants in one single operation on co-financing requirements?

Under financial instrument rules, national co-financing of a programme may be provided either by the managing authority or at the level of HF, or at the level of specific funds, or at the level of investments in final recipients, in accordance with the Fund specific rules. When the national co-financing is provided at the level of investments in final recipients, the body implementing financial instruments shall keep documentary evidence demonstrating the eligibility of the underlying expenditure. Financial instrument rules apply also to the grant part of the combination.

For financial instruments, eligible expenditure will be the total amount of programme contributions i.e. the sum of the Funds and national co-financing. In this case, co-financing refers to the external financing provided for the same investment and excludes project promoter's already available resources ('own contribution'). However, raising national co-financing for grants from private resources from the beneficiary's own contributions is a common practice, in particular in the SME sector. It is therefore worth stressing that when grants will be combined with a financial instrument in one single operation in the 2021-27 period, this way of co-financing will not be possible anymore.

In the examples below, the use of private co-financing at different levels is possible only if the co-financing rate at the level of the priority axis is calculated on the basis of total eligible expenditure.

Figure 9: Co-financing requirements financial instrument combined with grants



- At Holding Fund level, additional resources may be raised in order to provide the required co-financing to the combined financial instrument and grant instrument operation. This co-financing may be provided by the managing authority to the HF (using own budgetary resources or reflows from financial instruments implemented in past programming periods) within the funding agreement or the HF may use its own resources (if any) or raise external ones for this purpose, in the form of debt for instance, to contribute to the financial instrument.
- At specific fund level, FInt. are typically required to provide a financial contribution to the financial instrument with their own resources and thus this may ensure (at least partly) the co-financing of the operation. Financial intermediary's own contribution is usually required for State aid reasons (e.g. GBER on risk financing requires specific levels of private financing depending on the growth stage of the SMEs targeted by the financial instrument). FInt.'s co-financing thus contributes to the leverage effect of the financial instrument as well as ensures an alignment of interest between the MA and the FInt.

- At project level, existing resources from the final recipient cannot be considered as co-financing of the programme since the programme support - i.e. EU funds and national co-financing - have to be 'paid to' final recipients to be eligible. Additional resources - in the form of a bank loan or a capital increase for instance - which would be raised by a company to co-finance the eligible investment project could be treated as co-financing under the financial instrument-grant combined operation, as it would be triggered by the financial instrument and paid to the final recipient by the external financier. In the case of legal entities (in particular SMEs), a distinction should be made however between resources already forming part of the legal entity's assets and new assets transferred to the legal entity by its shareholders – e.g. a capital increase through the incorporation of reserves should not be eligible co-financing, but a capital increase through the issue of new shares with corresponding paid-in capital should be considered as additional private funding counting as national co-financing, provided that this capital increase is directly related to the investment being supported also by the financial instrument.

In any case, co-financing requirements need to be ensured at priority axis level within programmes and therefore a fully ERDF-supported combined financial instrument operation remains possible.

9. When will it be advisable to combine financial instruments and grants in two operations in the 2021-2027 programming period?

In view of the rules contained in the CPR for the 2021-2027 programming period, combinations where the vast majority of the projects require an amount of grants higher than the investments supported by the financial product will only be possible in two operations. This may happen in sectors traditionally heavily dependent on grant funding, where some marginal repayable forms of financing will be introduced. Another example is Energy Performance Contracting, notably when the grant will go to the building owner and the loan will go to the ESCO. In this case, it is advisable to have the combination made in two operations as the investment decision and the financing decision are clearly separated. Generally, when there is a need for a grant provided by the MA, the combination in two operations may be used.

5.2 Implementation phase

10. How will FInt. be remunerated to manage combined financial instruments and grants?

In the case of combinations of financial instruments and grants in two operations in which the grant is provided through a global grant/micro-grants system, the beneficiary may use a part of the global grant to cover its management costs and fees. In the 2021-27 programming period, when grants and financial instruments are combined in **one single operation, management costs and fees are calculated on the combined amount of grants and financial instruments**, which enables to compensate the bodies implementing the financial instrument for the additional management costs incurred for grants.

11. Do final recipients have to participate in a grant call when grants and financial instruments are combined in one operation?

No, the application of financial instrument rules to the grant component when combined in one financial instrument operation entails the use of a single application process for final recipients to get financing from the financial instrument. This unique application process shall be similar to the one typically applicable to a financial instrument, i.e. an open ongoing procedure whereby final recipients can submit a demand for financing at any time based on a business plan or any other similar document.

12. In the case of a combined financial instrument in one operation, is the support received from the grant part necessarily linked to a support received from the financial product for each and every project?

This question refers more specifically to combinations in which the grant is not 'embedded' in the financial instrument product, such as technical support grants and capital grants aimed at covering the non-revenue generating part of the investment. Loan interest rate and guarantee fee subsidies as well as capital rebates can be considered as being 'embedded' as the grant cannot exist separately from the financial product.

In the 2021-2027 period, the provision requiring the programme contribution in the form of grants to be lower than the amount of the investments supported by the financial product should be verified at the financial instrument level. This allows for the situations where the grant support would be higher than the investment part supported by the financial product **at project level**. This would be for instance the case when a project promoter benefits from a technical support subsidy but does not subsequently receive support from the financial product because the project is stopped or another source/ form of support is used. This may also be the case when the share of grants in the combined financing provided by the financial instrument needs to be increased for a specific and limited subset of the final recipients in order to ensure that the financial instrument achieves a higher policy impact. For instance, low-income borrowers may benefit from a (significantly) higher share of grants than other final recipients in multi-apartment energy efficiency retrofit projects to achieve higher energy efficiency levels through the investment. In all cases, the grant element shall remain linked and necessary to the financial instrument.

13. How will payments be made for grants combined with financial instrument in one operation?

A specificity of financial instrument is that payments are made 'up-front' to final recipients and not 'in arrears', i.e. not when the investment has been implemented and the project is completed. In the 2021-2027 programming period, the same rule will apply to grants combined with financial instruments in one operation, i.e. it will also be possible to pay the grant element 'in advance'. Combined disbursements (possibly in tranches) may be made by the body implementing the financial instrument to the final recipient before the project is completed. This will however remain a decision of the managing authority. The grant element may still be paid at different stages in the financial instrument lifecycle and will possibly be paid on behalf or directly to the final recipient.

14. In the case of a loan financial instrument combined with a performance-based grant, what would happen if the loan part of the financial instrument is disbursed shortly before the end of the eligibility period?

Grants may be provided as part of the same financial package after the end of the eligibility period (after 31 December 2029) on the basis of the Article 68 1(a) 2021-2027 CPR, which deals with the continuity of the financial instrument. This article states that 'where a financial instrument is implemented across consecutive programming periods, support may be provided to, or for the benefit of, final recipients, including management costs and fees, based on legal commitments made under the previous programming period, **provided that such support complies with the eligibility rules of the subsequent programming period**. In such cases, the eligibility of expenditure submitted in payment applications shall be determined in accordance with the rules of the respective programming period'. This provision however implies that FInt. are initially selected for a period potentially exceeding the programming period and may continue to provide financial instrument support in the following one as described above. This should therefore be anticipated in the selection process.

15. What should be the role of the body implementing the financial instrument in terms of grant decision?

The 2021-2027 CPR states that 'Financial instruments may be combined with programme support in the form of grants in a single financial instrument operation, within a single funding agreement, where both distinct forms of support shall be provided by the body implementing the financial instrument'.

HF and FInt. are bodies implementing financial instruments. Therefore the above mentioned provision allows either a HF or a FInt. to manage the grant element in case of a combination with a financial instrument in one operation. This provides some organisational flexibility and may not oblige banks acting as FInt. to manage grants in all cases if they are reluctant to do so.

In practice, some potential implementing bodies may indeed already have experience in managing grants, performing eligibility checks and assessing related projects. Some Member States' National Promotional Banks have implemented financial instruments combined with State budget-funded grant schemes for years. Other National Promotional Institutions may be willing to take on such responsibilities and to develop internal capacity.

Let us take the example of an urban development financial instrument combining a loan financial product and a capital grant. The ex-ante assessment of this financial instrument demonstrates that the capital grant element is linked and necessary to the financial instrument so that it can finance projects with a material impact but struggling to be financed on the market due to their higher risk or lower financial return. In this example, the managing authority directly entrusts a HF to implement the financial instrument. The HF then selects commercial financial institutions to manage the financial instrument, i.e. to select and finance eligible investment projects. However, during the market testing exercise, it appears that commercial banks, though recognising the importance of the grant element for the viability of the investments, are reluctant to manage it due to a lack of internal capacity and skills. In this case, the grant part of the combined financial instrument can be managed by the HF as a body implementing the financial instrument. A coordinated management system needs to be put in place between the commercial banks and the HF to ensure an efficient implementation. Financial instrument rules still apply to both the grant and financial product components of the financial instrument.

In this regard, the 2014-2020 combinations in two operations have identified some key success factors for an efficient coordination between the body managing the grant and the one managing the financial product:

- a careful planning of the required input early in the process, especially in terms of workflow organisation, is required.
- the development of a suitable IT system for the assessment and processing of applications as well as the production of the required documents and the storage of the necessary files is recommended.
- a continuous interaction between the FInt. and the HF manager needs to maintained.

16. Could some grant-related tasks be executed by a third party in a single financial instrument operation?

2021-2027 CPR does not provide a legal basis for any delegation of the grant related tasks by the body implementing the financial instrument to a third party. However, while managing the financial product and/or the grant, the bodies implementing the financial instrument may contract some tasks with external service providers, notably when specific technical skills or capacity is required. A FInt. could for instance sub-contract the project evaluation to a third party while keeping the responsibility to decide on the grant. This would allow the FInt. to access the necessary technical skills without having to develop them internally. Moreover, the grant decision could be automatically linked to the outcome of the outsourced technical assessment. The most obvious example would be the provision of an independent energy audit. In this case, the managing authority would define in the funding agreement the level of grants to be given in line with the improvement of the energy label achieved thanks to the new investment. The implementing body would use external energy audits as a proof of the investment performance and 'automatically' provide (or not) the grant element on this basis.

17. How and at what stage should the grant intensity in the combination of financial instruments and grant be decided?

The need for grants and financial instruments combined in one operation shall be identified and justified in the programmes and may be further assessed in the ex-ante assessment. On this basis, the funding agreement signed with FInt. will cover the grant and financial product and may quantify the two parts. The latter should reflect the expected average funding structure of the investment projects to be supported. It is however recommended that this split remains indicative and allows for variations during the implementation phase based on the actual applications received from project promoters. At this stage, (at least) two models may be used:

- a '**fixed grant' model**, whereby the grant intensity will be determined ex-ante in line with investment types or sectors or will depend on the attainment of measurable targets (see EE loan capital rebates). In this case, there is no room for interpretation and the decision can be automatized. This scheme may mitigate the risks of moral hazard related to the management of grants by FInt., if any.
- a **'tailored grant' model**, whereby a project by project evaluation of the grant intensity will be performed. In this case, a detailed financial evaluation of the project's funding and business plan will be carried out to define the adequate amount of grant needed. This may typically be the case for capital grants for large scale RDI or urban development projects. This task cannot be automatized and will require the allocation of adequate resources at the financial instrument or HF level.

From the point of view of commercial FInt., there may a preference for standard grant levels, which would be determined ex-ante in relation to objective and quantifiable criteria. In this case, guidance or methodology from the managing authority should provide certainty to FInt.. It may however be, like in the case of the Greek housing renovation programme, that FInt., once getting used to the financial instrument and after having collected experience, would request more flexibility in determining grant amounts to address final recipients' diversity.

Besides, implementing bodies with developed staff capacities and/or track record in managing publicly-supported financial instruments may be more willing/able to carry out project by project evaluations and be more inclined to manage more complex grant schemes. Typically, National Promotional Banks and International Financial Institutions may have this capacity. From a cost point of view, this may however only be worthwhile for larger scale projects.

18. What will be the reporting obligations for managing authority and FInt. applicable to grant and financial instrument combinations?

In terms of reporting, separate records will need to be maintained for each form of support, i.e. the grant and financial instrument. The body implementing the financial instrument combined with the grant should ensure a distinct accounting and reporting of the two forms of support. The reporting format for the grant will be aligned with the financial instrument's requirements. In comparison to the 2014-20 programming period, two specific lines in the reporting will be added for grants combined in one financial instrument operation as follows:

- **Data on the operation:** Information whether financial instrument is combined with programme support in the form of grants in a single financial instrument operation according to Article 58(5) 2021-2027 CPR.
- Other financial instrument specific information: Amount of private and public resources mobilised in addition to the Funds, by product: loans; guarantees; equity of quasi-equity; **grants within a financial instrument operation. This is based on the new provision regarding Annex VII, table 8 and reporting obligations**. One should report not only co-financing but also, in some cases, all public/private resources mobilised, including public/private resources, which do not constitute national co-financing. The purpose of this information is to allow the EC to calculate the achieved leverage.

The information to be provided by the managing authority is described in the Table 8 of appendix VII of CPR (see annex of this report). For the FInt., data is to be stored electronically and transmitted to the managing authority. The objective is that the managing authority stores and records electronically (in a system or systems) financial instrument related data for the purposes of monitoring, evaluation, financial management, verification and audit.

19. Will the declaration of eligible expenditure to the EC be split not only by 'priority/ region' but also by 'forms of support/funding' under the single financial instrument operation?

The declaration of expenditure for payment to the EC will not be split by form of support since grants and financial instruments are mixed as indicated in the model of the payment claim. The co-financing rate for EU funds applies at the level of the priority. The split is however needed in the reporting in order to be able to comply with the audit obligations (separate records per form of support).

20. How will audit principles apply to grant and financial instrument combinations?

According to the audit methodology applicable to financial instruments: 'the scope of the audit work should cover the risks related to:

a. the tasks undertaken by the managing authority at different stages of the financial instrument set up and implementation,
b. the work performed by the bodies implementing the financial instrument, the Fund of Funds (FoF), if applicable, and all or some financial intermediaries and
c. the eligibility of final recipients.

All these risks have to be covered through the audit work performed at the level of the MA and the bodies implementing the financial instrument and not at the level of the final recipient.'

Financial instrument audit principles will also apply to the grant element if combined in one single operation. The body implementing the financial instrument combined with the grant will need to keep track of the financed projects in the same way as for a financial instrument but will be required to keep separate records for the funding coming from the grant and from the financial product. This means that **no audit will be performed at the final recipient level on the grant element if it is combined in one operation with a financial instrument. Auditors will therefore not look and perform on the ground checks at the level of the final recipient.** The provision existing in the 2014-20 CPR according to which audits of financial instrument could be performed at the final recipient level in duly justified cases is not included in the 2021-2027 CPR anymore.

21. Does the managing authority have to make public the final recipients of financial instrument support in the list of operations according to the CPR article 49, paragraph 3? What if the grant element in the individual exceptional cases on the level of final recipient is higher than part of the investment supported by the financial product form the financial instrument, will it influence the applicability of the article 49, paragraph 3?'

In the case of a financial instrument operation, the 'beneficiary' is the body that implements the holding fund or, where there is no holding fund structure, the body that implements the specific fund (financial intermediary), or managing authority in case of direct implementation. Art. 49 (3) 2021-2027 CPR requires, in the case of legal entities, the publication of, among others, the beneficiary's name, i.e. of either the body that implements the holding fund, the specific fund or of the managing authority. Art. 49(3), however, does not require the publication of the name of the final recipients. This will not be different in cases where the grant component is higher than the amount of the investments supported by the financial product in a combination in one single operation, as financial instrument rules will continue to apply.

CPR, ANNEX VII, TABLE 8: Financial instruments data for the Funds

Priority[5]	Characteristics of expenditure			Eligible expenditure by product				Amount of private and public resources mobilised in addition to the contribution from the Funds			
	Fund	Specific objective	Category of region[7]	Loans (form of support code for FI)	Guarantee (form of support code for FI)	Equity or quasi-equity (form of support code for FI)	Grants within a financial instrument operation (form of support code for FI)	Loans (form of support code for FI)	Guarantee (form of support code for FI)	Equity or quasi-equity (form of support code for FI)	Grants within a financial instrument operation (form of support code for FI)

Amount of management costs and fees declared as eligible expenditure, including (MCF are to be reported separately in case of direct award and in case of competitive tender)[6]:						Interest and other gains generated by support from the Funds to financial instruments referred to in Article 54	Resources returned attributable to support from the Funds as referred to in Article 56	For guarantees, total value of loans, equity or quasi-equity investments in final recipients guaranteed with programme resources and actually disbursed to final recipients
Management costs and fees for holding funds depending on the financial product operating within the holding fund structure			Management costs and fees for specific funds (set-up either with or without the holding fund structure) by financial product					
Loans	Guarantees	Equity	Loans	Guarantees	Equity			

5 In the data exchange system SFC2021 the column should separate possibility to report MCF paid in case of direct of award of contract and in case of competitive tender.
6 It does not apply to the Cohesion Fund, AMIF, BMVI, ISF and EMFAF

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